

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS

FOR THE MINNESOTA DEPARTMENT OF COMMERCE

In the Matter of the Application

Filed by Hugh J. Janzen, Gary J. Benik,
Rodney Rangen, and Kenneth L. Kellar on
Behalf of Security State Agency of
Aitkin, Inc. for a Certificate of
Authorization (Bank Charter) in the Name
of Cook County State Bank, Grand Marais,
Cook County, Minnesota.

FINDINGS OF FACT,
CONCLUSIONS OF LAW,
AND RECOMMENDATION

The above-captioned matter came on for public hearing before Administrative Law Judge Steve M. Mihalchick on November 23, 1993, in the Grand Marais Community Center Social Room, Grand Marais, Minnesota. The hearing continued on November 29, 1993 through December 1, 1993, at the Department of Commerce Hearing Room, 133 E. 7th Street, St. Paul, Minnesota. Hart Kuller, Edward J. Drenttel, Jeffrey R. Ansel, and Karl Webber of Winthrop & Weinstein, 3200 World Trade Center, 30 East Seventh Street, St. Paul, Minnesota, 55101, appeared on behalf of the Applicants. Thomas S. Fraser, F. Chet Taylor, and John G. Kost of Fredrickson & Byron, P.A., 1100 International Centre, 900 Second Avenue, Minneapolis, Minnesota 55402, appeared on behalf of the Objector, Grand Marais State Bank.

The record closed in this matter on January 25, 1994, following the submission of post-hearing briefs and replies by the parties.

STATEMENT OF ISSUES

1. Whether the applicants are of good moral character and financial integrity.
2. Whether there is reasonable public demand for the proposed bank in this location.
3. Whether the probable volume of business in this location is sufficient to ensure and maintain the solvency of the proposed bank and the solvency of existing banks in the locality.
4. Whether the proposed bank will be properly and safely managed.

Based upon all the proceedings herein, the Administrative Law Judge makes the following:

FINDINGS OF FACT

Procedural Findings

1. On July 16, 1993, Hugh J. Janzen, Gary J. Benik, Rodney Rangen, and Kenneth L. Kellar formally filed an application on behalf of the Security State Agency of Aitkin, Inc. for a Certificate of Authorization (Bank Charter). The bank charter applied for would authorize a new bank, to be called the Cook County State Bank. The proposed location for this bank is a facility built at 6 West Wisconsin Street, Grand Marais, Minnesota.
2. Notice of the application was published in the Cook County News-Herald on July 26, 1993. A copy of the notice was sent by certified mail, return receipt requested to every bank and trust company within three miles of the site for the proposed bank.
3. On September 1, 1993, an objection was filed by Grand Marais State Bank to the application for a bank charter for the Cook County State Bank. Grand Marais State Bank requested that an administrative hearing be held.
4. James E. Ulland, Commissioner of Commerce, issued a Notice of and Order for Hearing setting a contested case hearing pursuant to the Administrative Procedures Act, Minn. Stat. 14.01 - 14.69. The first hearing date was set for November 23, 1993.
5. An abbreviated Notice of and Order for Hearing in this matter was published in the Cook County News-Herald.

Security State Agency of Aitkin, Inc.

6. The Security State Agency of Aitkin, Inc. (SSAA) is a bank holding corporation entirely owned Kenneth L. Kellar. SSAA owns 93.36% of the Security State Bank of Aitkin (Aitkin Bank). Kellar has never taken a dividend from SSAA or been paid a consulting fee by SSAA. The proposed bank would be 100% owned by SSAA.

Cook County State Bank

7. A facility has been built to house the proposed Cook County State Bank in downtown Grand Marais. In addition to the lobby, vault, and offices, the facility has an automatic teller machine (ATM) accessible after normal operating hours, a walk-up window, and a drive-through window. The second floor of the facility has work areas, a conference room, and an area designed for use as living quarters. The only exit from the living quarters is through the bank lobby.

8. The new bank would be run by a board of directors. The directors are Hugh J. Janzen, Rodney Rangen, Gary J. Benik, John Solien, Chris J. Nicolaision, and Dwain L. Moe.

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9. Janzen is President, Chief Executive Officer (CEO), and chairman of the board of the Aitkin Bank. He is also a shareholder in the Aitkin Bank and President of SSAA. Janzen began his banking career in 1961 as a bookkeeper. He advanced to teller, assistant cashier, assistant vice president, vice president, and senior vice president. In 1977, Janzen joined the Aitkin Bank's board of directors. Janzen became President of the Aitkin Bank in 1991. He has completed one year of the Minnesota School of Banking Program at St. Olaf's College. Janzen is a member of the Minnesota Banker's Association, the Independent Community Bankers of Minnesota, and the Independent Bankers Association of America.

10. Benik is the Vice President/Cashier for the Aitkin Bank. He first obtained that position in 1987. Before coming to the Aitkin Bank, Benik held the Vice President/Cashier position with the Battle Creek Bank of Saint Paul, Minnesota. Benik was involved with the initial start-up of the Battle Creek Bank, implementing the bank's electronic data processing, policies, and procedures. Prior to starting-up the Battle Creek Bank, Benik was the deposit operations manager for Norwest Bank at its Old St. Anthony branch.

11. Nicolaision is the owner of CS Service, Inc., the Chevrolet and Oldsmobile dealer in Grand Marais. He also operates a gasoline and heating oil distributorship. Nicolaision has been in business in Grand Marais for fifteen years.

12. Moe was the Finance and Insurance Manager for Benna Ford of Two Harbors from 1987 to 1993. From 1968 through 1987, Moe worked for the Commercial State Bank of Two Harbors, Minnesota. Moe started as a Bookkeeper and was promoted to the positions of Cashier and Vice President. In 1978, Moe became President of the Commercial State Bank. In 1983, Moe added the title of Chief Operating Officer (COO). In 1986, the COO title was removed, and Moe reported to another officer of the bank. In late 1986, Moe was demoted from President to Senior Vice President and he was given the title of Vice Chairman (of the board of directors). On November 11, 1987, Moe resigned both from the Board of Directors and as Senior Vice President.

13. During his tenure as an officer at the Commercial State Bank, Moe was not disciplined or informed his performance was unacceptable. His salary was never reduced. Moe's last performance review was done by Commercial State Bank's President, Rick Magnuson. That review rated him superior in customer

relations and delegation of authority; satisfactory in job knowledge, judgment, imagination, employee relations, attitude, and leadership; and below standard in quality, volume, initiative, and dependability. Exhibit O-47. The over-all performance rating put Moe in the middle of the "satisfactory" rating range. Id. The review specifically identified Moe's lack of formal education and training as weaknesses. The review recommended that any loans written by Moe be reviewed before approval. That same review assessed Moe as a "very capable MLA & ILA loan officer and can improve with add'l personal effort & training." Exhibit O-47.

14. Dean C. Johnson is the majority shareholder and CEO of Commercial State Bank. Johnson was dissatisfied with Moe's performance. Specifically, Johnson wanted Moe to inform himself of new banking rules and be more aggressive in his approach to banking. At no time during the years after Moe became President of the Commercial State Bank was the bank in financial difficulty.

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Aitkin Bank

15. SSAA was acquired by Kellar on July 2, 1991. That holding company has a 93.36% majority shareholder interest in the Aitkin Bank. When Kellar acquired the Aitkin bank its total assets were \$41.8 million and its return on average assets was 0.69. By June 30, 1993, the Aitkin bank's total assets were \$50 million and the bank's return on average assets had risen to 1.18. The average allowance for loan losses from 1989 through 1992 was 1.07. The level of adversely classified loans was \$2.03 million in 1986, dropping to a low of \$0.84 million in June, 1991. Adversely classified loans rose to \$1.7 million by June, 1992, and decreased to \$1.5 million by June, 1993.

Grand Marais State Bank

16. The Grand Marais State Bank is located at Second Avenue and Wisconsin Avenue in Grand Marais, Minnesota. The Cook County State Bank facility is located one block away. VH Bancorporation owns 93.75% of the Grand Marais State Bank. The remaining shares are divided among 20-25 others. VH Bancorporation is owned by John Von Holtum. In 1990, the bank had \$15.5 million in loans, had \$24 million in deposits, had a net income of \$334,000, paid \$180,000 in dividends, and paid \$47,000 in consulting and directors fees to Von Holtum. VH Bancorporation receives a percentage of the dividends paid equal to its percentage of ownership in the Grand Marais State Bank (93.75%).

17. In 1991, the bank paid \$300,000 in dividends and \$47,000 in consulting and director's fees to Von Holtum. The same totals were paid in 1992. From January through the end of September in 1993, a dividend in the amount of \$1.1 million was paid. Over that same period, \$58,500 was paid to Von Holtum in director's and consulting fees.

18. In December, 1992, the Grand Marais State Bank ranked 10th out of 637 banks in Minnesota in profitability measured as the percentage of return on average assets. Siemsen/Clayton Report, Exhibit R. The Grand Marais State Bank ranked 15th by that measure in December, 1991. Id.

19. A branch of the Grand Marais State Bank was opened in the town of Tofte, twenty miles southwest of Grand Marais along the north shore of Lake Superior. The Tofte branch was added to improve the convenience for businesses, particularly resorts, in the Tofte area.

20. The total deposits for the Grand Marais State Bank were \$27 million as of June 30, 1992. Applicants' estimate of the period from 1993 through 1997 (which assumes that only the Grand Marais State Bank and the North Shore Federal Credit Union are present in Cook County) projects an annual increase of \$3.5 million in deposits. McGladrey & Pullen Market Feasibility Study, Appendix J. By this estimate, the total deposits at the Grand Marais State Bank will reach \$47 million by 1997. Of 1,330 written applications for loans over the past three years, the Grand Marais State Bank has turned down thirty-three.

North Shore Federal Credit Union

21. The only other financial institution in Grand Marais is the North Shore Federal Credit Union. The Grand Marais facility is a branch of the

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Silver Bay office for that credit union. The North Shore Federal Credit Union submitted a letter objecting to granting the Cook County State Bank application, but did not file a formal objection. No financial information was submitted by the North Shore Federal Credit Union indicating the effect on the credit union of opening another bank in Grand Marais.

22. The total deposits at the North Shore Federal Credit Union (both the Silver Bay office and the Grand Marais branch) have grown from \$15 million in 1988 to \$18 million in 1992.

Public Demand for Banking Services

23. A substantial number of persons attended the public hearing in Grand Marais. George Peet, long-time owner of a number of motels in the Grand Marais area and a former President of the local Chamber of Commerce, described his inability to obtain short-term loans from the Grand Marais State Bank. Peet also noted that the North Shore Federal Credit Union was not able to meet his lending needs, due to federal lending restrictions. Regarding the dependability of the Grand Marais State Bank, Peet stated:

The one thing we can count on -- count on of the bank is that

when we need a bank turndown to get a government loan we can count on them to turn us down, even if we are able to get other loans.

Public Hearing Transcript, at 15. The businesses operated by Peet (or his son) sought and obtained over \$2 million in loans and lines of credit from sources outside the community and in some cases outside the state. The loans and lines of credit were sought between 1986 and 1993.

24. Burton Krietlow is a retired professor from Wisconsin and a member of the board of directors for the Aging Trust Fund. Krietlow moved to Grand Marais in 1981. He was unable to obtain a home loan from the Grand Marais State Bank to accomplish that move. Krietlow obtained that financing from Norwest Bank in Duluth.

25. Bruce Kerfoot owns the Gunflint Lodge and a canoe outfitting business in the community. He expressed his satisfaction with the Grand Marais State Bank and supported its objection to the application by SSAA. Nevertheless, Kerfoot cited two instances where particular banking needs were met by outside sources; credit card processing and an out-of-state real estate transaction. Kerfoot expressed concern that another bank in the community would dilute the ability of the Grand Marais State Bank to meet the lending needs of local businesses.

26. Larry Boen, Architect, cited two experiences he had with the Grand Marais State Bank. The first was a loan request for the purchase of a computer-aided design system. That request was rejected immediately. The second request was made over a period of three months, including the drafting of a business plan. That request was also rejected. Boen did not seek outside funding for the proposed business project.

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27. Dennis Rysdahl, owner of the Bluefin Bay resort in Tofte, expressed satisfaction with the service provided by the Grand Marais State Bank. Rysdahl cited the Tofte branch as being convenient for both his business and his customers. He indicated that some of the buyers for his condominiums have obtained mortgage loans from the Grand Marais State Bank. Employees of the Bluefin Bay resort have obtained loans from the Grand Marais State Bank, much like credit union loans. The President of the Grand Marais State Bank assisted Rysdahl with placing a large commercial loan with First Bank of Duluth.

28. Chris Nicolaison, a proposed director for the Cook County State Bank, expressed his dissatisfaction with the Grand Marais State Bank in regard to automobile loans for his customers. The only in-house financing available for customers was originated out of Duluth. When Nicolaison sought a business loan, the President of the Grand Marais State Bank indicated the request would be denied, even before a written application had been made.

29. Jim Norvell came to Grand Marais in 1987. He obtained a Small Business Administration loan with the participation of the Grand Marais State Bank. Norvell expressed satisfaction with the services provided by the Grand Marais State Bank.

30. Kelly Bergstrom recounted her experience with the Tofte branch of the Grand Marais State Bank. She received a loan for her trailer home without difficulty.

31. John Conda operates a real estate company and is the current President of the Chamber of Commerce. He characterized the interest rates for home loans as "typically one to two percent higher than anyone else that's in the marketplace...." Public Hearing Transcript, at 64. Conda indicated that borrowers for such loans either used a credit union or a source in Duluth.

32. Conda also indicated that in the three to four months prior to the hearing, the Grand Marais State Bank has become much more visible through advertising and has joined a number of civic organizations.

33. John Lavine owned an automobile parts business in Grand Marais for eighteen years before he sold it last year. He related his impression that the Grand Marais State Bank has recently become "more sensitive to the community's banking and financial needs." Public Hearing Transcript, at 70. While he was in business, Lavine could get occasional loans, but much of his borrowing was done outside Cook County. Lavine's major personal account is with an out-of-town institution.

34. Edward Landin is a resident of Cook County who recently sold his resort business in the area. Landin has both his personal and business accounts in Two Harbors, Minnesota, which is over eighty miles from Grand Marais. He supported competition amongst banks in Grand Marais.

35. Bill Radek owns the funeral home in Grand Marais. He recounted the assistance received from the Grand Marais State Bank in invigorating the business he purchased in February, 1993. Radek noted that development is going on in Cook County which he characterized as "growing by leaps and bounds." Public Hearing Transcript, at 88.

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36. James Lashinski, owner of the IGA store (a supermarket) and part-owner of Steve's Sports & Auto, indicated that in his experience more established businesses received assistance from the Grand Marais State Bank but that less-established businesses went unserved. Lashinski noted an entirely different attitude of the Grand Marais State Bank toward the business community after the application of SSAA to open a bank became public knowledge.

37. A number of letters submitted during the application process have indicated loan requests have been rejected by the

Grand Marais State Bank without written loan requests having been filed. Many of the persons who testified or submitted letters indicated that they no longer make applications for loans since they believe the request will be rejected.

Economic Activity in Cook County

38. Cook County has a population of 3,868, with 1,171 persons living in Grand Marais. Cook County has 1,670 households, 31% of those households are located in Grand Marais. At any one time, 16,849 persons are present in the county on an overnight basis. The large number of nonresidents is due to the substantial tourism industry present in the county. The number of tourists is stable regardless of season due to the variety of activities available. Lutsen is a center for downhill skiing in the winter. The Gunflint Trail originates in Grand Marais and extends into the Boundary Waters Canoe Area (BWCA). The Grand Portage Casino is forty-five miles away and open year-round.

39. There are approximately 265 businesses located in Cook County. Thirty-five of those businesses have started within the past two years. Twenty-one businesses have expanded within that time. Retail sales totalled \$24,641,000 in 1990, almost double the total for 1985 (not adjusted for inflation). The gross sum of all good and services related to travel and tourism is \$89,800,000 for 1991, compared to \$49,900,000 in 1987.

40. The Superior National Golf Course opened in 1991, near Lutsen. Condominiums and vacation homes are being constructed near the golf course. An average of 197 building permits have been issued each year over the period from 1990 to 1992 in Cook County for residential, commercial and public construction.

41. Minnesota Planning for Population Change forecasts that the population of Cook County will decline from 3,868 in 1990; to 3,810 in 1995; 3,700 in 2000; 3,590 in 2005; 3,510 in 2010; 3,460 in 2015; and 3,400 in 2020. Exhibit O-44. Lee Maxfield, President of Maxfield Research Group, Inc., disputed the demographic analysis as to its accuracy and applicability in projecting the performance of a new bank in Cook County. Maxfield cited the increase in the number of households, the construction of additional seasonal housing, and an increase in the labor force (from 1,360 in 1980 to 1,903 in 1991) as reasons to forecast growth and additional need for financial services in Cook County. Exhibit A-15, Maxfield Report at 4.

Projected Performance of the Cook County State Bank

42. Initial capitalization of the Cook County State Bank consists of \$300,000 from common stock to be held by SSAA and \$2.7 million in surplus. The Cook County State Bank intends to pay no dividends during its first three years of operation.

43. By its first estimate, the Cook County State Bank

anticipated that it will obtain 10% of the total market for individual, partnership, and corporation (IPC) deposits for a total of \$3.5 million in the first three years of operation. An additional \$1.1 million was expected in nonconsumer deposits over this period.

44. The performance anticipated under the assumptions set forth in the foregoing Finding would result in the Cook County State Bank suffering losses of \$121,459 in the first year, \$24,947 in the second year, and \$20,041 in the third year. A revised estimate from the Applicants indicates losses of \$119,650 in the first year, \$23,110 in the second year, and \$18,157 in the third year. This revised estimate anticipates a profit of \$24,841 in the fourth year of operation.

45. Two additional estimates of performance were made using the aggregate method of estimating deposits (aggregate method) and the market penetration method of estimating deposits (penetration method). Siemsen/Clayton Report, at 5-9. Under the aggregate method, the Cook County State Bank would achieve total deposits of \$5.5 million at the end of three years of operation. The aggregate method uses household income and deposit data to establish a consumer deposit base and then estimates 10% of the market will go to the new bank. The amount generated from consumer deposits is expected to comprise 80% of the total deposits at the new bank. The remaining 20% is forecast to be business or public fund deposits.

46. The market penetration analysis arrived at a forecast of \$5.04 million in deposits after the first three years of operation. The penetration method estimates the new bank's share of market growth at 15% in year one of operation, 25% in year two, and 33% in year three. Siemsen/Clayton Report, at 9. This method was characterized as conservative, due to the level of financial activity being removed from Cook County. Id.

47. The profitability analysis as revised by the Applicants, dated April 1, 1993 shows losses of \$108,401 in the first year and \$10,234 in the second year. That analysis shows the Cook County State Bank earning profits of \$6,540 in the third year of operation and \$59,205 in the fourth year. Exhibit A-11.

48. An estimate of performance for the new bank provided by Grand Marais State Bank estimated losses of \$125,508 in the first year, \$43,026 in the second year, and \$35,067 in the third year. Enger Opinion, Appendix A, page 16. The Objector's estimate anticipates a profit of \$27,241 in the Cook County State Bank's fourth year of operation. Id. These estimates are based upon the methodology used for calculating costs and the deposit growth assumption used by the Applicants, both criticized by the Objector as "unrealistic." Enger Opinion, at 6.

49. The Grand Marais State Bank estimates IPC deposits will grow by \$2 million per year in the Grand Marais Area. Murphy Opinion at 14. The \$2 million estimate is based solely on the experience on the Grand Marais State Bank and the North Shore Credit Union. Id. at 13. In arriving at the projection for IPC

deposits available to both the Grand Marais State Bank and the Cook County State Bank, the possibility of drawing deposits from the North Shore Federal Credit Union was expressly excluded. Murphy Opinion, at 14.

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The estimate does not take account of whether any assets currently taken outside Cook County would become available to the Cook County State Bank.

50. The Cook County State Bank estimates that noninterest income will amount to \$33,000 in the first year of operation, \$86,000 in the second year, \$114,000 in the third year, and \$167,000 in the fourth year. Noninterest income is revenue from check-printing, traveler's checks, service charges, and other fees. The income from this source, calculated as a percent of average assets is .84% in the first year, 1.53% in the second year, 1.58% in the third year, and 1.85% in the fourth year. Enger Report, at 9. The Grand Marais State Bank criticized the anticipated income from this revenue source. The average income from this source for Minnesota banks of less than \$10 million in total assets is .8 percent of average assets. *Id.* The Aitkin bank has .47 percent of its average assets in revenue from this source and the Grand Marais State Bank has .77 percent of its average assets in revenue from noninterest income. There are four banks which have achieved 1.85% of noninterest income. *Id.*

51. The Cook County State Bank projected its allowance for loan losses as 1% of total loans. The Grand Marais State Bank objected to this percentage as too low. Murphy Opinion, at 9. The average for banks of less than \$20 million in total assets is loan losses of 1.74% of total loans.

52. The living quarters situated on the second floor of the facility prepared for the proposed bank are subject to a rental agreement from SSAA which pays the Cook County State Bank \$15,000 per year, as rental for the use of the living quarters. The Grand Marais State Bank objected to the transaction as having no economic substance. Enger Opinion, at 11. James G. Miller, Deputy Commissioner of Commerce, suggested during the initial application process that the Cook County State Bank lease the space to avoid having the start-up bank bear the cost of these accommodations. Exhibit A-1, Letters from the State of Minnesota, at 4.

Whatcom State Bank

53. In 1989, the Whatcom State Bank was under a cease and desist order for poor management issued by the State of Washington. In that year, Kellar invested approximately \$0.75 million dollars to become the Whatcom State Bank's majority shareholder. Kellar replaced the board of directors, replaced the bank president, and changed the procedures in use at the Whatcom State Bank. Kellar has not taken a dividend or been paid

a consulting fee by the Whatcom State Bank.

54. When Kellar took over ownership of the bank, it had \$9 million in deposits. Kellar described \$5 million of those deposits as "hot money" meaning that it was not appropriate to consider that money as a bank asset.

55. By the end of 1993, the Whatcom State Bank had total deposits of \$47 million. Two branch offices had been opened. Annual independent audits from 1991 suggested modifying procedures used by the bank to account for its transactions and identifying a potential "Regulation O" violation. That regulation sets standards for loans to bank insiders. Exhibit O-13. The Whatcom State Bank management responded to the comments from the audits. By 1993, the audit showed significantly fewer material weaknesses in the

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procedures used by Whatcom State Bank and noted improvements in many areas of the bank's procedures.

Application Answers

56. On the personal history portion of the application, Kellar listed his education level as grade 12. His formal education ended at the eighth grade. Kellar made no mention of his involvement at the Minnesota resort where the 1950's era lawsuit was filed. Kellar did not fully describe his import/export business, nor did he mention that he was involved in gaming enterprises in the recent past.

Based on the foregoing Findings of Fact, the Administrative Law Judge makes the following:

CONCLUSIONS

1. The Administrative Law Judge and the Commissioner of Commerce have jurisdiction of this matter pursuant to Minn. Stat. 46.041.

2. Proper notice of the hearing in this matter has been given.

3. The applicants are of good moral character and financial integrity.

4. There is reasonable public demand for the proposed bank in this location.

5. The probable volume of business in this location is sufficient to ensure and maintain the solvency of the proposed bank and the solvency of the Grand Marais State Bank and the North Shore Federal Credit Union.

6. The proposed bank will be properly and safely managed.

Based upon the foregoing conclusions, the Administrative Law Judge makes the following:

RECOMMENDATION

IT IS RESPECTFULLY RECOMMENDED THAT:

The Application filed by Hugh J. Janzen, Gary J. Benik, Rodney Rangen, and Kenneth L. Kellar on behalf of Security State Agency of Aitkin, Inc. for a Certificate of Authorization (Bank Charter) in the name of Cook County State Bank, Grand Marais, Cook County, Minnesota, be GRANTED.

Dated: March 4th , 1994.

/s/

STEVE M. MIHALCHICK
Administrative Law Judge

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Duluth, Minnesota
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MEMORANDUM

The issues to be determined in this proceeding have been set forth in the Notice of Hearing. Each issue will be discussed in this Memorandum.

Moral Character and Financial Integrity

The Objector has questioned the moral character of the primary shareholder of SSAA, Kenneth Kellar. These questions have focussed on Kellar's answers in the personal history portion of the application, the operation of other banks owned by Kellar, two legal matters involving Kellar, and the proximity of the proposed bank to the Indian-operated casino in Grand Portage.

Kellar did not correctly state his level of education. There is no educational standard which must be met to own a bank. The difference between an eighth grade education and a twelfth grade education is not critical for a person in his sixties who has extensive business experience. While Kellar's statements in the employment history portion of the application could have been more accurate and complete, the information contained there was

not misleading.

Kellar has maintained the other banks he owns (through holding companies) in good condition. Indeed, the management of both the Aitkin Bank and the Washington Bank appears to have improved after Kellar obtained the status of majority shareholder.

The two legal matters cited by the Objector are a failed real estate transaction in 1993 from the State of Washington and a lawsuit in Minnesota dating back to the late 1950's. The Washington transaction was a dissolution of partnership. The troubling aspect of that deal was the partnership's application to one of Kellar's banks in Washington for a \$50,500 commercial loan. Kellar's participation in the partnership was not mentioned to avoid insider ban requirement. This matter is troubling, but not sufficient reason to deny the application. The Minnesota lawsuit is over twenty-five years old and not indicative at all of Kellar's moral character.

The Objector has implied some sinister connection between Kellar's banking activities in Washington, Indian-operated casinos, and the Canadian border. See Exhibits O-41 and O-42. Kellar has operated money exchanges between Canadian and U.S. currency. Kellar has provided services to Indian-operated casinos. Kellar has been involved in gaming enterprises in South Dakota. Kellar owns several banks. All of these enterprises are legitimate business ventures. The record in this matter is lacking any evidence that an illegitimate enterprise is being operated by Kellar.

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Perhaps most important to the question of moral character is Kellar's track record at the Aitkin Bank and the Washington Bank. There has been no indication that Kellar lacks the moral character necessary to own a bank and generally review its operation. Clearly he operates his businesses and personal life in a manner that adds greatly to the communities in which he does business. No questions were raised regarding the moral character of the other directors or officers of the proposed Cook County State Bank.

Reasonable Public Demand

The statutory standard for a bank charter, that there be "reasonable public demand," was examined in *Jackson v. Valley National Bank*, 152 N.W.2d 472 (Minn. 1967). Twelve factors (the Jackson factors) were considered to determine if reasonable public demand exists. These factors are:

- (1) Number of banks already serving the area in which the proposed bank would locate;
- (2) size of area;
- (3) population of area;
- (4) wealth of residents of area;
- (5) commercial and

industrial development of area; (6) potential growth of area; (7) adequacy of the services being provided by existing banks compared to the needs of residents and the services to be offered by the proposed bank; (8) capability of existing banks to handle potential growth of the area; (9) convenience of the location of existing banks to residents of the area as compared to convenience of the proposed bank; (10) size of banks in the area; (11) dates when the banks in the area were established; and (12) the number of the persons in area who desire to use the proposed bank and the amount of business they would generate.

Jackson, 152 N.W.2d at 474 (citations omitted).

Only one bank is located in Cook County. Other banks are serving that area to the extent that customers go outside the area to obtain services, but this fact does not diminish the noncompetitive nature of banking in Cook County as it is currently practiced. A credit union has a branch in Cook County, but significant limitations exist on the ability of a credit union to issue loans and otherwise meet local needs.

The geographic size of the area is large. To reach the nearest bank outside the area, a customer must drive eighty miles from the site of the proposed bank. For customers in Grand Portage, Minnesota, the drive would be over one hundred miles. The permanent population of the area is small, but not exceedingly so. The temporary population is vastly larger than the residential population. The median income of the residents in Cook County is slightly below that of similar counties in Minnesota, but the business activity and development in the area is substantial with potential for continued significant growth.

The services provided by the existing banking facilities are adequate, in the sense that loans are available, deposit services are available, and other banking services are available. The steady and substantial growth of deposits at the Grand Marais State Bank indicates that some of the growth in economic

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activity in Cook County is reflected in that bank's performance. However, banking services are inadequate to the extent that loans are denied to persons who are credit-worthy, but do not meet the high standards for loan approval imposed by the Grand Marais State Bank. The number of persons who indicated that they bank outside Cook County is evidence that the existing bank is not providing adequate services to meet current demand. The existing facilities are inadequate to give local customers the benefit of local competition.

The potential for continued growth of business in Cook County is great. The Grand Marais State Bank is large enough and financially capable to meet the demand for additional services. However, that bank has not indicated that it is willing to adapt

its business practices, absent direct competition. The North Shore Federal Credit Union's branch in Grand Marais is not large, but has performed well in the last few years.

The Grand Marais State Bank and the local branch of the North Shore Federal Credit Union have been in existence for a sufficiently long period to ensure that both are established financial institutions. Neither is at risk of insolvency due to the opening of a new bank in Grand Marais.

Despite the limited population of Cook County, a large number of people have expressed interest in having a new bank open in Grand Marais. Many of the persons expressing interest are business people who are likely to direct substantial demand toward the new bank. Considering all the Jackson factors, there is reasonable public demand for a new bank in Grand Marais.

Solvency

An extensive feasibility analysis supports the conclusion that a new bank will attract enough deposits and loan business to remain solvent. Use of the aggregate or penetration methods of assessing future performance are appropriate. Under those approaches, the Cook County State Bank will be profitable at the end of the third year of operation. While the assumptions underlying the new bank's feasibility study are, in the main, optimistic, they are not unreasonable. The loan loss rate of 1.0 in the study was criticized as too low, but the average loan loss rate over three years for the Aitkin bank was 1.07.

The rental income to the Cook County State Bank for the second-floor living area was criticized as an improper arrangement by the Grand Marais State Bank. The inclusion of living quarters on bank premises is unusual. The cost of furnishing the space was borne by Kellar directly and the rental arrangement was expressly made to avoid having the start-up bank bear a cost which would directly benefit the owner. The rental arrangement was suggested by regulators and is not improper.

The Objector asserts that loan participations are improperly included in the solvency forecast. Loan participations were added in the last revision of the Cook County State Bank's forecast and are necessary for that bank to show a profit in three years. The Grand Marais State Bank asserts that if loan participations are necessary, then reasonable public demand does not exist for the new bank. The Objector has blended three concepts to make this argument. Reasonable public demand is the desire for a new bank, only one factor of which is the actual amount of money that will go to that bank. Solvency does not rely upon any particular level of earnings, merely that the bank will be

able to meet its obligations. Profitability within three years is a Federal Deposit Insurance Corporation (FDIC) standard, not a

standard for granting or denying an application for a bank charter. The loan participations were forecast to meet the FDIC standard and appear overly optimistic. Nonetheless, they are a legitimate means of enhancing income. But in this case, they are irrelevant to the solvency of the Cook County State Bank.

Even accepting the Objector's analysis, which projects a very conservative growth in deposits in Cook County, the Cook County State Bank will be solvent. The analysis shows that the Cook County State Bank would not render a good rate of return on the initial investment made to capitalize the bank. The statutory standard to be met is solvency, not any particular level of profitability. While the forecast relied upon by the Objector bank is based upon assumptions which do not reflect the true potential for economic growth in Cook County, even if that forecast was to be accepted, the application cannot be denied on the basis of insolvency by the new bank.

The Grand Marais State Bank was profitable at a much smaller size than it is today. The addition of a new bank is not likely to reduce the size of the Grand Marais State Bank, merely reduce that bank's rate of deposit growth. The probable volume of business in Cook County is sufficient to ensure and maintain the solvency of the Applicants' new bank and the solvency of the Grand Marais State Bank and the North Shore Federal Credit Union.

Proper and Safe Management

As discussed above in this Memorandum, the owner of the proposed Cook County State Bank is experienced in the banking industry and has had success with several banks. All of the directors of the proposed bank have extensive business experience. The directors who have worked at the Aitkin bank have long experience in banking. The proposed President for the new bank, Dwight Moe, has nearly twenty years of experience in banking.

Two aspects of the proposed management for the Cook County State Bank bear discussion. First, Moe's employer in his last banking position criticized Moe for failing to keep up with banking regulations. Moe had not done anything by the date of his pre-hearing deposition to become reacquainted with current banking regulation. Moe has strengths in dealing with people, but weaknesses in technical compliance. Second, Moe has tentatively hired his nephew as Cashier for the new bank. The nephew has no experience in banking whatsoever. These are legitimate concerns, and more significant in a start-up bank.

The Cook County State Bank has proposed two approaches to remedy any shortfalls which may occur in this area of management. First, the directors from the Aitkin Bank will be spending substantial amounts of time with the Cook County State Bank during the first six months of its operation. One director has experience with start-up banks and he will be amongst those directors on hand. Second, consultants will be made available to add expertise to the operation of the bank and "fill in" any areas not covered by the President or Cashier. If carried out,

these two actions will ensure that the Cook County State Bank is properly and safely managed. While the cost of consultants will reduce the profitability of the new bank, that cost will not affect its solvency.

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The experience demonstrated by Kellar in operating the Washington bank shows that he is capable of changing personnel where required to make a bank profitable. There is no indication on the record of this matter to suggest that Moe will be retained as President if he cannot properly operate the Cook County State Bank.

Conclusion

Cook County has a growing economy and will be materially aided by the addition of a new bank. The residents of Cook County will benefit from meaningful local competition. The proposed bank is properly capitalized and overseen by experienced directors. The applicants are of good moral character and financial integrity. The proposed bank will be safely and properly managed. There is a good deal of public demand for a local competing bank. The demand is sufficient to render all banking facilities in the area, including the proposed bank, solvent. Therefore, the Judge has recommended that the Application for a bank charter for the Cook County State Bank be GRANTED.

S.M.M.

